

**City of Mesa**  
**Deferred Compensation Committee**  
**MEETING MINUTES**  
**Monday, November 3, 2014, 11:30am**  
**Mesa City Plaza, Suite 130**  
**Personnel Conference Room 2**

**Members Present:**

Mike Kennington (Chair)  
Don Miller  
Derek Witting  
Mary Dellai  
Michele Long  
Vicki Eden

**Members Absent:**

Frank Hoglund  
Kimberly Call  
Michael Claspell

**Innovest:**

Jerry Huggins  
Wendy Dominguez

**Great West:**

Scott Taylor  
Lisa Tilley

**Other(s):**

Bill Taebel  
Nikki Rosales  
Gary Petrytus-Galloway

**Meeting called to order at 11:35am by Mike Kennington**

**1. Approval of the August 4, 2014 minutes**

Don motioned to approve the minutes  
Michele seconded the motion  
None opposed

**2. Innovest Quarterly Update**

**The Markets**

Last quarter everything was positive and this quarter only large U.S. stocks and bonds were positive. Developed international, emerging markets and small cap stocks were all negative, with small caps as the worst place to be at -7.36%.

**Headwinds/Tailwinds**

Global growth is disappointing, as Continental Europe faces a new recession and exports slow for China. The U.S currently has the highest bond yields, but overall bonds yields are expected to remain low. The strength of the U.S. dollar has been a huge tailwind. The U.S. economy continues to improve with unemployment at a low, home prices up and gas prices falling.

**Quarterly Market Summary**

Overall, commodities were down 12%, emerging markets and developed international were negative, and S&P 500 was one of the highpoints for the quarter. In the U.S. sector, energy and utilities were down this quarter and the best performance was in healthcare and technology. All areas of the international equity region had negative performance for the quarter.

### U.S. Equities Chart

A new chart was added to the update, showing the volatility of U.S. equities. The chart shows the S&P 500 actual return for the calendar year, as well as how much the index was down at some point within the year. It's not uncommon for the index to be negative at some point and still end up positive for the year. The average intra-year drop is about 14% over the last 34 years. The market feels more volatile than the numbers actually indicate.

### Annual Fee Review

Updated as of 6/30/14, the average asset total over the last 12 months was \$157,962,241. All plan expenses total 58 basis points, which is very good compared to similar plans.

### Asset Allocation

Plan assets increased about \$340,000 during the quarter. Participant allocations maintain stable. The brokerage window continued to increase, but not as much as it did last quarter.

### Table of Returns

Healthcare and technology did well this quarter, but utilities and energy struggled. The large, mid and small cap equity managers had decent performance relative to the benchmark and their peers, except for Aston Montag & Caldwell Growth, as well as Kalmar Growth-with-Value Small Cap. Both funds have high quality managers that emphasize quality holdings, and growth is not in that area right now. Managers on the international side had negative absolute performance in the quarter, but were at median or benchmark performance on a relative basis. Over the 1-year period, all international equities have absolute positive performance and are above median. Global equity was right at the benchmark and ranked in the 29<sup>th</sup> percentile. The plan's emerging markets fund was negative, but lost less than the benchmark and outperformed the median manager. On the fixed income side, PIMCO underperformed the benchmark and its peer group and ranked in 91<sup>st</sup> percentile. The global real estate fund underperformed and ranked in the 93<sup>rd</sup> percentile for the quarter, but they are currently back in the top quartile. High yield is right at benchmark, even though it had a negative absolute return. Stable value is right at median and it's crediting rate looks good compared to high quality stable value funds. All vintages in the target date funds had negative performance last quarter, but the year to date and 1-year numbers show positive performance. All model portfolios had negative performance, but were in line with their benchmarks. Their 1-year numbers show they are slightly trailing their benchmarks.

## Manager Scorecard

	Organization	People	Philosophy & Process	Style Consistency	Asset Base	Performance	Expense	Overall
Fidelity Contrafund					Minor concern			
Aston: M&C Growth						Major concern		Minor concern
Mainstay; Lg Cap Growth	Minor concern	Minor concern						
Artisan: Mid Cap					Minor concern			
Kalmar: Gro/Val SC						Minor concern		
Voya: GIBL RE	Minor concern					Minor concern		Minor concern
PIMCO Total Return	Minor concern	Major concern						Minor concern
Mesa/GW Custom Stable Value			Minor concern					

Minor concern  
 Major concern

- **Kalmar: Gro/Val SC** – poor performance of 2014 has weighed heavily on the long-term performance. Cumulative 3 & 5-year periods are now below median and benchmark.
- **PIMCO Total Return** – had a minor concern in organization when Mohamed El-Erian resigned. Bill Gross is now leaving, so a major concern for people and a minor concern overall have been added.
- **J Hancock Mid Cap** – minor concern for organization was removed
- **American Funds EuPc** – minor concern for asset base was removed

## New Watch List

Watch List Criteria	MainStay Large Cap	Aston Montag & Caldwell	Kalmar Growth-with-Value Sm Cap	PIMCO Total Return	Voya Global Real Estate
NUMBER OF QUARTERS ON THE WATCH LIST	5>	5	1	3	5>
Changes in Ownership Structure or Material Litigation	Minor concern			Minor concern	Minor concern
Investment Management Team Changes	Minor concern			Minor concern	
Significant Increase/Decrease in Assets Under Management					
Investment Style Stable/Consistent and Adherence to Investment Guidelines					
Performance In-Line with Expectations		Minor concern	Minor concern		Minor concern

*All shaded boxes indicate a FAIL in that criteria*

- **Aston Montag & Caldwell** – has now been on the watch list for 5 quarters
- **J Hancock Disciplined Value Mid Cap** – removed from the watch list
- **Kalmar Growth-with-Value Small Cap** – added to the list for Performance In-Line with Expectations
- **PIMCO Total Return** – added Investment Management Team Changes to the watch list

### 3. Review Watch List Report on Aston/Montag & Caldwell Growth

This fund was added to the plan in January 2013 to replace Rainier Large Cap Equity, but has been on the watch list for 5 quarters. It was added to compliment MainStay Large Cap Growth, because the two funds have different management styles. Due to their emphasis on high quality holdings, this manager will not perform well in the current environment, but will perform better when you want a more defensive manager in place. This manager has made some mistakes though, such as having zero weight in Apple. At this time, Innovest is not concerned with the fund, because it is performing the way they would expect it to, in this type of environment.

It was mentioned that the performance definition in the Investment Policy Statement reads as: performance should be in-line with expectations, as measured by cumulative, risk-adjusted, annual, and rolling three-year performance against benchmark and peer groups. It is hard to compare this type of management style against the benchmark, so the committee asked to see a peer comparison at the next quarterly meeting. In addition, the description on the watch list may need to be changed to assess generic performance, rather than performance expectations.

The committee was all in favor to continue to watch this fund and compare its performance against its peers at the next meeting.

### 4. Core Fixed Income Mutual Fund Search

Innovest had a site visit with PIMCO and spent a lot of time there with the managing directors. Believe they are probably the best-equipped manager on Wall Street to be able to withstand such a significant loss of a key person, but there are still uncertainties that surround the current team. Innovest suggests looking at other candidates, in place of PIMCO.

Fidelity Total Bond	Metropolitan West Total Return Bond	Dodge & Cox Income
<ul style="list-style-type: none"><li>• Firm Inception 1946</li><li>• Firm Assets \$1.3 trillion</li><li>• Strategy Inception 2002</li><li>• Strategy Assets \$16 billion</li><li>• Expense Ratio 0.45%</li><li>• Revenue Sharing 0.10%</li><li>• 3 portfolio managers with 77 analysts</li><li>• Strategy includes both a top-down &amp; bottom-up approach</li><li>• Tend to stay close to what the benchmark is</li></ul>	<ul style="list-style-type: none"><li>• Firm Inception 1971</li><li>• Firms Assets \$141 billion</li><li>• Strategy Inception 2000</li><li>• Strategy Assets \$42 billion</li><li>• Expense Ratio 0.40%</li><li>• Revenue Sharing 0.10%</li><li>• 4 portfolio managers with 20 analysts</li><li>• Ownership concern-In 2013 was acquired by a private equity firm, Carlyle Group</li><li>• Carlyle Group appears to keep employees of other firms they have taken over</li><li>• True team approach with value-based process</li></ul>	<ul style="list-style-type: none"><li>• Firm Inception 1930</li><li>• Firm Assets \$224 billion</li><li>• Strategy Inception 1989</li><li>• Strategy Assets \$78 billion</li><li>• Expense Ratio 0.43%</li><li>• Revenue Sharing N/A</li><li>• 9 portfolio managers with 22 analysts</li><li>• Bottom-up strategy, look at individual securities to add value</li><li>• Less diversification can lead to a lumpy performance</li></ul>

The committee reviewed the pros and cons and all funds presented. Consistency counts showed how well each fund did against their benchmark and the median, over the last 10 years.

Mike motioned to move funds from PIMCO Total Return to Metropolitan West Total Return Bond

Derek seconded the motion

None opposed

## **5. Great West Quarterly Update**

### Third Quarter Update for 2014

There were a few changes to the plan this quarter. DFA Emerging Markets Fund was added to the core investment lineup. Loans have switched to auto-approval. GW now has all necessary information to assure loan policy rules are met, so they no longer require city sign off. Pay contribution limits lowered to 75%, based on Payroll feedback. This will prevent participants from putting 100% of their check into the plan, allowing enough remaining funds to cover their benefits. Lastly, Great-West completed the acquisition of JP Morgan Retirement Plan Services.

Plans assets grew very little and are now at \$162,433,236. The total number of plan participants is at 2,843, which is the largest growth that has occurred in a while. More employees are signing up at new hire orientation now. Contributions were huge in the third quarter, but that number includes drop rollovers. The net cash flow for the quarter was \$1,531,936. Payroll contributions were at \$2,768,138 for the quarter, with incoming rollovers at \$1,434,685, most of which were from the public safety pension. There were 57 new loans and 20 full withdrawals in the quarter. There were only two unforeseeable emergency withdrawals and no death benefits claims.

### NAGDCA Comparison

The comparison was updated with the 2014 NAGDCA results, which included 86 governmental 457 plans. Mesa's total plan participation rate is 62.5%, which is lower than previous years, but probably a more accurate number. The NAGDCA average was 49%. The average plan participant account balance for NAGDCA was \$57,000, whereas Mesa's was \$55,556. Mesa's average participant annual contribution was \$4,984 and NAGDCA's was \$4,250.

### Investment Advisory Services Usage

The plan offers three levels of investment services: Guidance, Advice and Managed Accounts. There was no change to usage of the advice option, which remained at six participants, but the managed account usage increased to 439 participants.

### Local Education

Scott was available a total of 34 days in Mesa. He held 11 group meetings, 2 educational seminars, 29 individual meetings and 4 new employee orientations.

### On the Horizon

There are two new enhancements coming to the website on November 5, 2014. One is a new investment research tool, where all the information you would want about investments will be on one page in an easier format. The second enhancement will be an update to the “Transfer My Investments” process. Participants indicated that the previous process was difficult, so these changes should make it easier. GW also plans to roll out an enhancement to the website login process. The new process will include login phrases and pictures to improve security. This has generated phone calls from the customers that have already received the enhancement, so it will be rolled out in stages to their remaining clients. The last change to expect is that Putnam and the former JP Morgan RPS will be integrated with Great-West and will be rebranding to Empower Retirement.

### **6. Upcoming Meetings**

Next quarterly meeting will take place on February 2, 2015

### **7. Meeting Adjourned at 12:45pm**